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Technical Director
Financial Accounting Standards Board
401 Merritt 7, P.O. Box 5116
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director@fasb.org

Re: File Reference No.2012 -260: Proposed Accounting Standards Update, *Financial Instruments – Credit Losses (Subtopic 225-15):*

Mayer Hoffman McCann P.C.(MHM) appreciates the opportunity to comment on the Proposed Accounting Standards Update (ASU) on *Credit Losses* (Exposure Draft).

MHM believes that the Exposure Draft and the proposed change to an expected loss model from the incurred loss model will add complexity and cost to financial reporting which is not offset by any significant measureable benefit. While we understand users concerns regarding the incurred loss model, we do not believe moving to an expected loss model will provide any significant added benefit in most instances. The current incurred loss models used by reporting entities rely heavily on historical data that is updated for changes in the economic environment and changes in the underlying characteristics of the financial instrument. We believe the implementation of an expected loss model would result in similar volatility as the expected losses would be based on similar data. The "too little, too late" concerns would not be significantly different under the expected loss model, which is evident in the fact that the fair value of financial instruments, which incorporates market participant assumptions regarding expected losses, did not forecast the significant losses brought on by the financial crisis until the same time as those expected losses were incorporated into reporting entities current incurred loss model assumptions. It would be unrealistic to expect reporting entities to predict all expected losses until confirming events which are different from historical results actually occurred, indicating the losses should be expected.

Estimating Credit Losses vs. Fair Value

We are concerned with the operational implementation of reporting entities internal methods used to estimate the expected credit losses and the interaction of those internal methods and models with the estimated cash flows from a market participant perspective as required by Accounting Standards Codification 820, *Fair Value Measurement*. While we believe the current incurred loss model provides the most appropriate model for recognizing credit losses as they occur over the life of the instrument, we believe fair value provides a superior model as compared to the expected loss model in the Exposure Draft, primarily due to concerns over comparability. We would encourage the

FASB to revisit the incurred loss model and perhaps consider if a reduction in the probable threshold provides a better potential alternative to addressing the concerns associated with "too little, too late".

Should the FASB move forward with the Exposure Draft, we believe the FASB should consider providing additional guidance with respect to estimating the cash flows under the expected loss model and how such a model should compare to the estimated cash flows for the same instrument from a market participant perspective (i.e. fair value). We believe there may be confusion regarding the recognition of day one gains or losses from acquired financial instruments when the cash flows under the expected loss model, which are determined by the reporting entity differ from the cash flows that would be used to determine fair value from a market participant perspective.

In many instances, entities may acquire a financial instrument or pool of financial instruments in a purchase transaction which are believed to be undervalued by the market due to temporary market displacements or other changes to credit spreads. In such situations, it would be unlikely the reporting entity would record an allowance for credit losses for some time after the acquisition, if ever. We are unsure if that will be the expectation of the FASB or financial statement users, particularly when the market has placed a discount on the instrument due to credit concerns. Additionally, if a reporting entity's expected loss model and market participant expectations result in different cash flow estimates on the date of acquisition through a purchase transaction, would an additional day one loss be considered appropriate? As such, we believe there will be similar confusion and questions regarding the timing and expectations of recording of an allowance for credit losses for loans receivable (or similar instruments) upon the acquisition of such instruments through a purchase transaction.

It would be beneficial if the FASB would provide additional clarification regarding the expectations of whether the estimated credit losses used to determine fair value from a market participant perspective are expected to be the same as a reporting entity's internal cash flow assumptions on the date of acquisition.

The Exposure Draft allows a practical expedient for certain assets measured at fair value through other comprehensive income (OCI). We believe there is little, if any, benefit to recording an allowance for credit losses for an instrument measured at fair value. We believe this will lead to confusion and inconsistencies between cash flows measured using internal models and those of market participants used to determine fair value. This model would result in impairment losses recorded using internal cash flow models while the instrument is recorded at fair value using market participant estimates. We believe the practical expedient should be applied to all instruments measured at fair value through OCI when expected credit losses are expected to be insignificant (as determined based on carrying value, not par or contractual value). To avoid confusion, if expected credit losses are expected to be significant, the impairment should be recorded based on market participant expectations. If the appropriate measurement model for an instrument is fair value, we do not believe providing differing cash flows estimates (one using market participant expectations and one using internal modeling) is beneficial, and in fact creates unnecessary confusion.

We agree that subsequent changes to the estimated cash flows associated with purchased credit impaired loans should result in an adjustment to interest income or net interest margin. However, the Exposure Draft allows the allowance for credit losses to be determined using internal cash flow models. Again, it is unclear how differences in estimated credit impairment between internal models and those based on market participant expectations should be treated on the date of acquisition.

Differences could result in significant "day one" adjustments to the fair value on the date of acquisition through adjustments to the allowance for credit losses.

AS stated above, for these reasons, we believe additional implementation guidance focused on the interaction of estimated cash flows used in determining ASC 820 fair value measurements and the expected losses model would be beneficial and would avoid potential confusion.

Impact to Private Companies

We believe it would be prudent for the FASB to seek the Private Company Council's review and consideration of the proposed Exposure Draft. Specifically, we believe the PCC should determine if exemptions for private companies which are non financial lending institutions should be considered. We believe the Exposure Draft will add unnecessary burden and complexity as it relates to trade receivables and related party receivables for private companies.

We appreciate the opportunity to provide comments on the Exposure Draft. Please contact Ernie Baugh or Michael Loritz if you have questions.

Sincerely,